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SIPDIS

TREASURY FOR FTAT AND OCC/EILEEN SIEGEL
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TREASURY PASS FEDERAL RESERVE, FINCEN, SEC/E.JACOBS

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SUBJECT: Austria Enacts Bank Rescue Package; Consortium
Rescues Small Constantia Bank

REF: VIENNA 1534 AND PREVIOUS

¶1. SUMMARY: On October 21, the Austrian Parliament unanimously approved an EUR 100 billion (\$130 billion) rescue package, with modest changes to the draft announced last week (reftel). The GoA will guarantee up to EUR 75 billion (\$97 billion) in loans (down from EUR 85 billion), will set aside EUR 15 billion (\$19.5 billion) in equity to be injected into banks if needed, and has earmarked EUR 10 billion (\$13 billion) to cover deposit guarantees. On October 17, the five major Austrian banks agreed to bail out the small Constantia Privatbank by injecting a GOA-guaranteed EUR 400 million (\$520 million) into the bank. END SUMMARY.

¶2. Due to the crisis, the outgoing Austrian Parliament convened a special session on October 21 to adopt the EUR 100 billion rescue scheme for Austrian banks (reftel). Parliament approved the package unanimously but with a few changes following negotiations over the weekend:

- The new state guarantee for interbank lending was scaled back from EUR 85 billion to EUR 75 billion.

- The GOA can inject up to EUR 15 billion total into banks and insurance companies in case of liquidity problems. The GoA will have the option to buy shares of banks and insurance companies and the Ministry of Finance can even nationalize banks (partially or fully) to avoid systemic damage (a "last resort" according to FinMin Molterer). The GOA is more likely to raise bank capital increase through preferred shares with no voting rights, to minimize government influence. GOA shares must be privatized as soon as market conditions allow it, but there is no time limit.

- The GoA will earmark EUR 10 billion to cover individual bank deposits. The new law foresees that banks will guarantee assets of private and business account holders up to EUR 50,000 (\$65,000), including accounts of SME's with sales up to EUR 9.7 million (\$12.6 million). The GoA will guarantee unlimited individual deposits until the end of 2009. As of 2010, the GoA will guarantee individual savings up to EUR 100,000 (\$130,000).

¶3. Most major Austrian banks still insist that recapitalization is not needed -- nobody wants to be the first one in line -- but experts expect the "big five" (UniCredit-Bank Austria, Erste Bank, Raiffeisen Zentralbank, Bawag and Volksbank) to take capital injections in a concerted action soon. Only Erste Bank has not ruled out a state capital injection to date. On October 21, a member of the board of the National

Bank advised banks to take government financial assistance.

¶4. The first Austrian bank to stake a guarantee claim is the small "Constantia Privatbank" (CPB), mainly active in private banking and real estate assets. CPB, which was to be sold to Credit Suisse earlier this year for around EUR 1 billion, suffered a liquidity collapse in recent weeks. UniCredit, Erste, Raiffeisen (25% each), Bawag and Volksbank (12.5% each) agreed to take over CPB and will inject EUR 400 million into CPB, which the GoA will guarantee. The National Bank added another EUR 500 million (\$650 million). NOTE: Reportedly, the banks did not rescue CPB voluntarily but only under GoA pressure, which feared negative consequences. The "big five" have their own private banking departments and have no use for the CPB's assets, so they may liquidate CPB soon if they do not find a buyer. END NOTE.

¶5. CPB had balance sheet assets of around EUR 1.2 billion (\$1.5 billion), oversaw about EUR 10 billion (\$13 billion) of client assets, and employed 260 people. The bank's majority owner, Christine de Castelbajac, may be forced to pledge the assets of her industry group Constantia Packaging (worth EUR 350 million) to CPB's rescuers. Observers debate whether CPB was a victim of the financial crisis or collapsed purely due to mismanagement. The bank's collapse stemmed from its ties to two troubled real estate funds ("Immofinanz" and "Immoeast") led by CPB CEO Karl Petrikovics and whose deposits CPB managed. The funds'

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share prices plummeted from over EUR 7 to less than one euro within six months. Insiders including the bank's owner reportedly withdrew their assets prior to CPB's fall.

Modest Economic Stimulus En Route

¶6. The caretaker GoA has agreed on the outline of an economic stimulus package that could be approved at the first session of the newly elected Austrian parliament next week. Proposed measures include expanding credit guarantees for SME's (from EUR 2 to 3 billion), EUR 150 million (\$195 million) in subsidized loans for SME's, and commissioning infrastructure projects (primarily rail/road construction) worth EUR 1 billion over the next four years. The full package is worth about 1% of Austrian GDP.

COMMENT

¶7. The EUR 100 billion financial rescue package is huge, representing over a third of Austria's GDP (EUR 260 billion in 2006) if fully utilized. GoA representatives insist their guarantees will not come due, but the fact that the GoA rushed to enact the package -- a week before the new parliament debuts -- might hint of unknown liquidity problems at banks. The collapse of the small Constantia Bank should not be overrated, but puts an additional burden on the other banks. The Austrian banks' heavy involvement in troubled Central and Eastern European states, particularly in Hungary and Ukraine, will have implications as will shrinking demand for Austria's exports. Elsewhere in Europe, economic growth forecasts or Austria are trending downwards (0.9 to 1.2 percent in 2009, per the Austrian Institute for Economic Research) and there are clear signs that Austria's strong labor market (3.6% unemployment in the 2nd quarter) will soon deteriorate.

